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SUBJECT: JCRED - PROGRESS REPORT

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Summary

1. (SBU) Summary. Significant progress has been made with Iraq in many economic policy areas since the July 10-11 Joint Commission on Reconstruction and Economic Development (JCRED) in Amman, Jordan. The Iraqis have moved toward the approval of their 2006 budget and beginning negotiations on an IMF Stand-By Arrangement. They are, however, behind on WTO accession, privatization, and moving to suspend implementation of the Arab League Boycott. The Iraqis have taken modest steps to strengthen their private sector, often in response to broad efforts by USG entities seeking to move the economy away from its statist orientation. End summary.

MACROECONOMIC AND STRUCTURAL REFORMS

2. (SBU) 2006 Budget: The Minister of Finance submitted his preliminary estimates for the 2006 Budget to the IMF as a follow-up to Iraq's Article IV consultations. The Council of Ministers has endorsed this 2006 budget, which will tackle politically difficult fuel and food subsidies by reducing budget allocations for these subsidies by 25 percent annually over 4 years. The TNA is expected to approve this budget in October. At the same time, the Government of Iraq (GOI) is working with the World Bank, USAID and donors to introduce social benefit and safety net measures, such as means-testing, so that the genuinely poor people will not be disadvantaged by reduced fuel and food subsidies. The Iraqis also are looking closely at ways they can increase oil exports and reduce refined fuel imports in order to increase revenues available to general budget use.

3. (SBU) IMF Stand-By Arrangement: During the World Bank/IMF Meetings in Washington on September 23 and 24, Iraq Finance Minister Allawi had productive discussions with IMF officials regarding Iraq's effort to secure a Stand-By Arrangement (SBA) with the IMF. The IMF announced on September 23 that it is working with Iraqi authorities to move toward a SBA as a follow-on to their Emergency Post-Conflict Agreement (EPCA). The IMF has approved starting negotiations with the Iraqis with the aim of completing the SBA by the end of the calendar year. The current Iraqi Government is expected to endorse a reform policy framework that will obligate the next government to implement in order to retain the benefit of the Paris Club debt reduction agreement.

4. (SBU) Debt Relief: Completion of an IMF Stand-By Arrangement will keep Iraq on track toward meeting its overall Paris Club debt reduction agreement. Of Paris Club creditors, only the U.S. and Canada have signed bilateral agreements. Since the July JCRED, the Government of Romania signaled its willingness to re-negotiate Iraq's debt in conformity with Paris Club principles, and on August 18, Romania's Ministry of Finance signed such a debt re-negotiation agreement with Iraq regarding \$2.5 billion debt (ref A).

5. (SBU) Banking Sector Reform: The Embassy (USAID and IRMO) are two months ahead of schedule in preparing the balance sheets of Iraqi state-owned banks as well as their executive summary assessment. Reform options for the banking sector will be presented to the Ministry of Finance by mid-November. USAID and Treasury are gathering financial information requested by the Minister of Finance to support the development of a state-bank reform program. We have begun to provide direction for

the work of the Minister of Finance via a new Joint Task Force on Budget and Finance, led by the Treasury Attache Taecker and the Minister of Finance Allawi. The first meeting on September 13 focused on expenditures in the 2006 budget. Treasury's interagency meeting with Iraqi officials on September 22 on the margins of the World Bank/IMF Meeting also helped to set the agenda and activities for the next task force meeting in Baghdad.

DONOR ASSISTANCE AND COORDINATION

16. (SBU) Currently, donor coordination is occurring on multiple fronts. The monthly Baghdad Coordination Group meeting between the Minister of Planning and Development Cooperation and Baghdad-based donor officials provides an effective forum for discussion and strategic level coordination. Second, sectoral working groups have been established for education and health, and soon will be established for electricity and rule of law. These working groups will be led by the Ministries of Education, Health, Electricity, and the Chairman of the Supreme Court. Third, the Iraq Strategic Review Board (ISRB) meets on a more regular basis to ensure that donor-funded projects are consistent with national priorities as articulated in the National Development Strategy (NDS). National priorities include those projects that are labor intensive and in essential services (i.e., water, electricity, road, bridges). The ISRB also seeks to ensure equitable regional distribution of donor funding.

ENERGY POLICY

17. (SBU) Draft Oil Law: The GOI has been taking steps to reform its energy policy by drafting a law to liberalize the import and distribution of refined fuel products (ref B). If adopted and implemented, the law would end the State Oil Marketing Company's monopoly on fuel imports by enabling foreign companies to import and sell certain refined fuel products. It is also our understanding that the Ministry of Oil intends by this law to liberalize the price at which imported fuel can be sold in Iraq, but the draft language on this point is ambiguous. The Minister of Justice is currently examining the draft law.

18. (SBU) Infrastructure Security: Multinational Security Transition Command-Iraq (MNSTC-I) has completed the training of the first four Strategic Infrastructure Battalions (SIBs). Training is underway for the next group and is expected to be complete in December. The primary duty of these units is protecting critical linear infrastructure such as oil pipelines and electricity lines. The GOI agreed in September to assume the cost (just over \$80 million) of maintaining these units.

PRIVATE SECTOR DEVELOPMENT

19. (SBU) SOE Privatization Plan: On August, 29, 2005, the Council of Ministers signed a Privatization Decree, which calls for the formation of a ministerial committee that will oversee the research, identification, and feasibility of privatizing state-owned enterprises (SOEs). The committee, led by the Minister of Planning and Development, will include the Ministers of Finance, Industry & Minerals, the Treasurer of the Central Bank of Iraq, the President of the Board of Supreme Audit, and a representative from the Prime Minister's Office. The committee will present its recommendations to the General Secretary of the Council of Ministers by the end of

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October 2005. USAID facilitated the development of the committee and continues to provide technical support on privatization, including developing an SOE database and SOE profiles at the Ministry of Minerals and Industry, as well as advising the Iraqis on how to address social safety net issues impacting redundant employees.

10. (SBU) Investment Promotion Agency: The Iraqi Investment Promotion Agency (IIPA), the establishment of which was announced at the JCRED, seeks to help Iraqi and foreign investors open businesses in Iraq. With the support of USAID, the IIPA is still in the process of becoming operational. Three ministries (Planning, Industry & Minerals, and Trade) are all involved in the staffing process. USAID has tentatively scheduled visits for the new staff of the IIPA to economic development agencies in Georgia and North Carolina in late October or early November.

11. Investor Roadmap and Competitiveness Study: Also in

the area of investment, USAID has put together an "Investor Roadmap" to be completed before the end of October. This document details the step-by-step process for foreign companies on how to invest in Iraq (i.e. register, taxes, etc). There is also a "Competitiveness Study" due out about the same time that highlights the industry sectors in Iraq that have a competitive advantage vis-a-vis competitors. Once these are completed, they will be housed at the IIPA as resources available to potential investors.

TRADE AND ASSISTANCE

¶12. (SBU) WTO Accession: The Ministry of Trade submitted Iraq's Foreign Trade Memorandum (FTM) on behalf of the GOI at the end of August 2005. USAID's Izdihar Project, which assisted with the development of the FTM, has developed a set of approximately 600 questions that it estimates Iraq will receive from the members of its WTO Working Party and is working with government officials to prepare them for WTO accession requirements. However, the GOI must take additional steps in upcoming months to maintain the momentum for its WTO accession. These steps include selecting a WTO Chairman for their Working Party, appointing a WTO ambassador, and assembling a delegation to attend the WTO Ministerial in Hong Kong in December 2005. Despite Post's pressure, the Iraqis have made little progress on these tasks. For example, the Minister of Trade has not appointed a new Director General to replace Ahmed al-Mukhtar, who previously headed Iraq's WTO efforts and was recently dismissed. The Deputy Director General, Abdul Salam, is currently running the office, but lacks the power to push WTO issues with Iraqi Trade Minister Karim.

¶13. (SBU) Iraqi Trade Information Center: USAID's Izdihar Project also has been working with the Government of Iraq to develop an Iraqi Trade Information Center that will be part of the Ministry of Trade and located at the Baghdad International Fair Grounds in Al-Mansour. It is modeled after the U.S. Department of Commerce's Trade Information Center and will serve as a one-stop-shop for private firms seeking information about trade and investment opportunities. The new center is scheduled to open by the end of November.

¶14. (SBU) Arab League Boycott: Post has engaged the relevant officials in the GOI, including at the highest level, numerous times over the past five months to press for non-implementation of the Arab League Boycott (ALB) (ref C). While enforcement of the Arab League Boycott is not/not mandatory for Arab League members, Law No. 34 of 1956 implements the ALB in Iraq. CPA Orders have suspended or removed ALB requirements in trademark and company registration processes. The Minister of Trade has indicated that he sent written instructions to the Council of Ministers regarding non-enforcement of the ALB. Nevertheless, ALB enforcement by the GOI appears to continue in other areas of the economy, e.g. refusing docking privileges for ships that have used Israeli ports. Post will continue to push the GOI on non-enforcement of the ALB, but the next JCRED provides an additional venue to press the GOI on this issue.

¶15. (SBU) Generalized System of Preferences (GSP) and Iraqi Dates: Iraq must take advantage of the GSP exception for certain categories of dates granted by the Administration on June 30, 2005. Iraq was a major producer and exporter of dates, which before the 1990's ranked a distant second to oil and related products in its share of Iraq's total exports (ref D). Post is now taking the next steps by finding interested Iraqi date exporters.

IMPLEMENTING AGREEMENTS FROM JULY JCRED

¶16. (SBU) Post delivered a letter to Vice President Mahdi on September 19 encouraging him to forward the three JCRED bilateral agreements (Trade and Investment Framework Agreement, Investment Incentive Agreement, and Economic and Technical Cooperation) from the Presidency Council to the TNA, with the recommendation that the TNA ratify them. Post is arranging a meeting with the TNA Speaker to stress the importance of these agreements. Satterfield